RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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June 17, 1998 **LETTER 1254**

June 5 DJIA 9037.71; PTI 5333; A-D Ratio +10.52
June 12 DJIA 8834.94; PTI 5328; A-D Ratio +9.59
Dow Yield: 1.61%; Dow Price/Earnings: 22.7
Dow 144-day MA: 8581; Dow 34-day MA: 8979
Dow Times Book Value: 5.54; PTI 89-day MA: 5302
Percentage of Undervalued Blue-chips: 4%
Gold 34-day MA: 299

EMOTIONS: I want to start this Letter off in a rather unorthodox (for me) way. In the latest issue of *Forbes* there are two articles that I zeroed in on. One article states that one should **always** be very heavily invested in the stock market. You see, looking back over history, it has paid a person, regardless of the market's position, to always be loaded with stocks. Stocks have done better than bonds, bills, cash or gold. And timing is impossible. Therefore, be loaded with stocks at all times. The second article states that asset allocation is the real answer. Yes, one should always have a portion of one's assets in stocks, but real estate, bonds, even gold may be worthwhile diversifications.

Frankly, I've read a lot of articles like these. Looking back over history, many experts have concluded that one should always be heavily invested in stocks. The real risk is in not being in stocks, because if you're not heavily in stocks you're going to be left behind when the big up-moves arrive. Therefore, forget timing, forget trying to avoid the declines and forget trying to catch the reversals, just be in stocks.

And I think to myself, that's logical thinking and great research, but these guys all leave out one vital ingredient -- and that ingredient is **fear**. I've lived through the bear markets of 1946-'49, 1957, 1966, 1968 and the disaster of 1973-'74, and I was lucky enough to avoid all of them. But believe me, when you see your stocks going down 40%, 50%, 70% and 90% you get sick to your stomach, you can't sleep nights, you berate yourself for being a "damn fool," you swear that you never want to hear about Wall Street, and stocks again.

Fear is the critical ingredient that these experts leave out when they talk about being "fully invested" at all times. They leave out the element of **naked fear.** They forget that people become frantic, half-crazy when they see their life-savings going down the drain. So what do these fearful people do when fear overtakes them? They sell their stocks at or near the bottom. Finally, believe me, the twin emotions of fear and greed are the two strongest emotions that you'll ever have to deal with in the market. But fear is an even stronger emotion than greed.

THE MARKET. I think the market's overvalued and I know there's a hell of a lot of mindless speculation going on. But the market couldn't care less about what Richard Russell thinks. Consequently, I'm going to bury my pride, and instead, I'll just let the Dow Theory and my **Primary Trend Index (PTI)** call the shots.

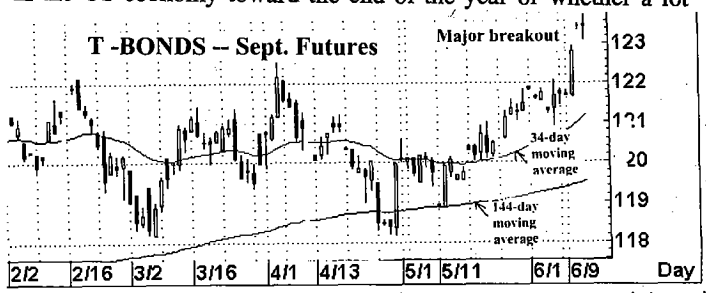
As this is written, the PTI is still in its bullish mode, which means the PTI is still holding above its 89-day moving average, although its moving progressively closer to that critical MA. Let me put it this way -- if or when the PTI turns weak and drops below its 89-day MA, I will turn bearish. At that point the bull will be unceremoniously yanked out of the Investment Position box, and in its place we will see a nasty, growling bear. But that has not happened yet -- which is the operative fact for me at this time.

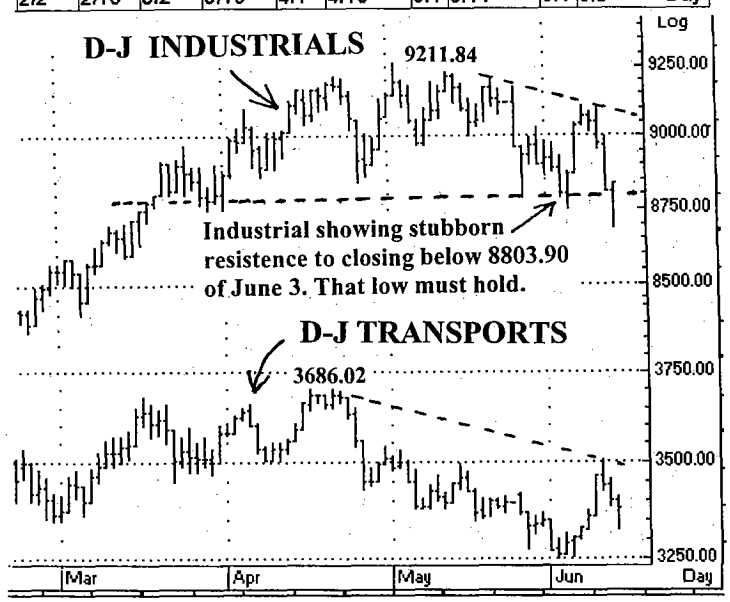
Around early June the stock market became severely oversold, with the market recording its decline lows on June 3. On June 4 strength came into the market and the Dow rallied strongly. This was followed by a further 167 point Dow surge on June 5. But by the middle of last week, the advance appeared to be slowing down -- possibly even fizzling. Question: Can the Dow advance to a new high above its record high of 9211? I guess it could, but if it does go to a new high it will probably go without confirmation by the Transports or the advance-decline ratio.

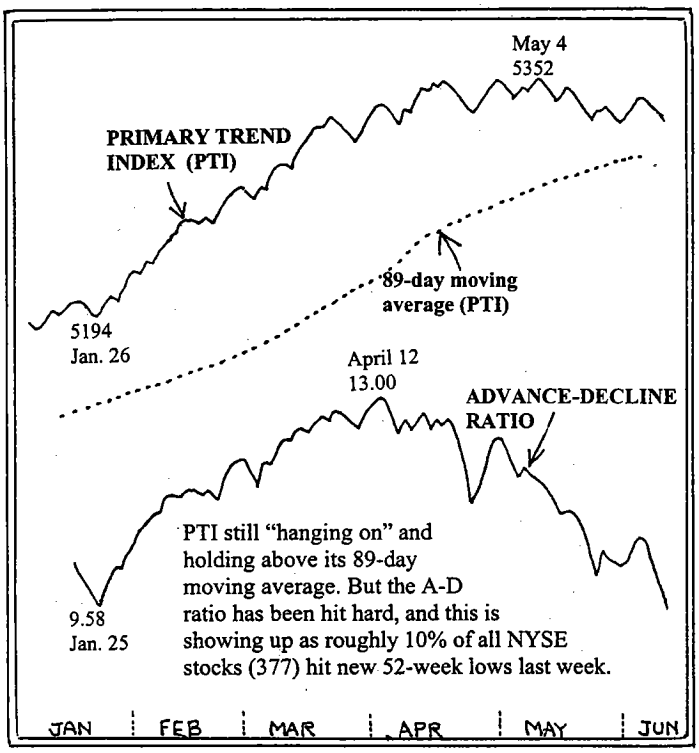
As I see it, the two most critical numbers in the market are (1) the June 15 Dow extreme low of **8684.22**, and (2) the June 3 S&P closing low of **1082.03.** As long as both of these lows hold, the bulls will have reason to be hopeful. But let both of these low break, and the bears will have smiles on the faces.

CHARTS: Back in the '60s they used to say, "The charts are never wrong, it's the people who read the charts who are wrong." With that thought in mind, let's study a few significant charts and see if we can, hopefully, get it right.

First, a chart of the September T-bond futures. The bonds hit their most recent important low on April 30 at 118 6/32nds. Since that time the bonds have rallied back to their highs, this despite the US unemployment rate at a 28-year low and a still-vibrant economy. Whether it's foreign money driving up the bonds or whether the bonds are discounting a major slowdown in the US economy toward the end of the year or whether a lot







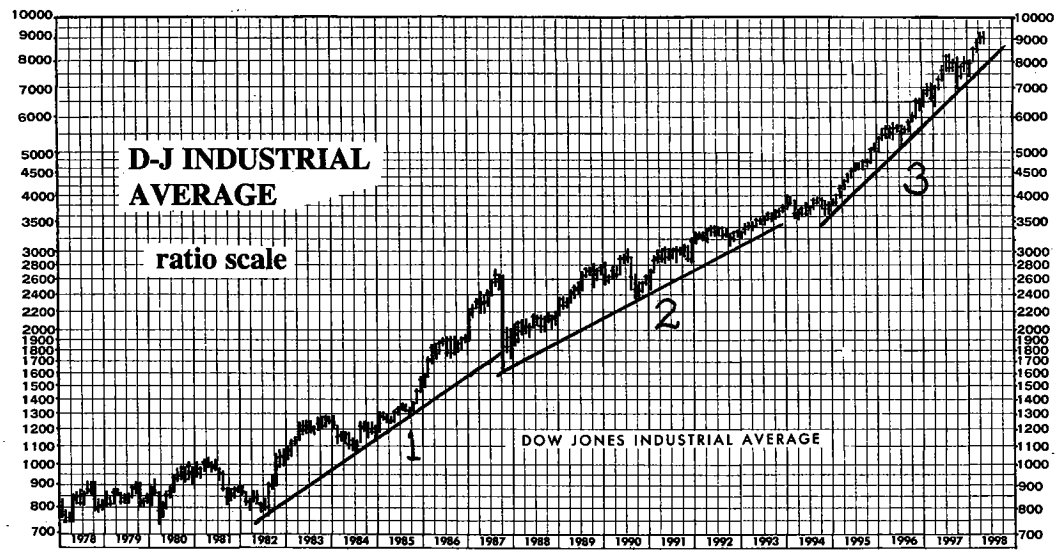
third rise dropped the yield on the Dow to a record low of 1.52%, a low never seen before during a bull market.

What can we gather from this extraordinary chart? First, the chart deals with three consecutive Dow advances, with the third being the most violent and speculative. During the third advance, stocks surpassed all known historical values. Historically, three major advances have often sufficed to complete a major bull market. This fact plus the overvaluation suggest that the third rise, as seen on this chart, may have about completed the bull market. Well, maybe.

Aside from these three huge advances, what do we really know at this point? We know that **the advance-decline ratio** topped out on April 12. This tells us that since April 12 the **majority** of issues on the NYSE have been in a declining trend. We know that the **D-J Industrial Average** hit its high of 9211.84 on April 13. We know that the **D-J Transportation Average** struck a record high of 3686.02 on April 16. We know that the **S&P 500** hit a record high on April 22 at 1130.00.

If we are still in a bull market then in due time all of the above marks will be bettered. On the other hand, if the bull market is building a top, then it will be many months, probably years, before we see these highs again.

Question: Russell, Fed chief Greenspan says that this nation is in great shape. What in the world could happen that would even hint at a bear market now or in the future?



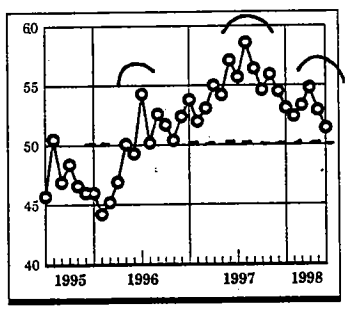
Answer: I could come up with many possibilities, but most of them would probably be wrong. The answer is that, invariably, the **reasons** for the beginning of a bull or a bear market are only realized months or sometimes years **after** they start.

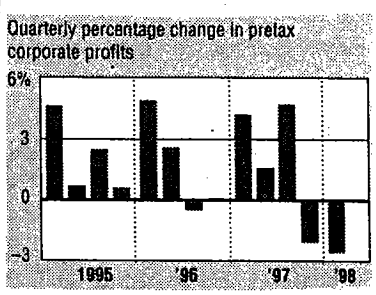
More charts: This first chart (*WSJ*) shows the widely-watched Purchasing Managers Index. These are the guys who buy the goods for the corporations, and they have to plan ahead. So what the Purchasing Managers are doing tells us quite a bit about forthcoming business activity. The index was 52.9 in April, and it dropped to 51.4 in May. Anything below 50 indicates that purchasing managers are beginning to "pull in their horns." What interested me here was that the index has assumed the form of a potential "head-and-shoulders" top. In other words, the pattern suggests that the index could shortly drop below 50%. If that happens, it will not be a good sign for the economy.

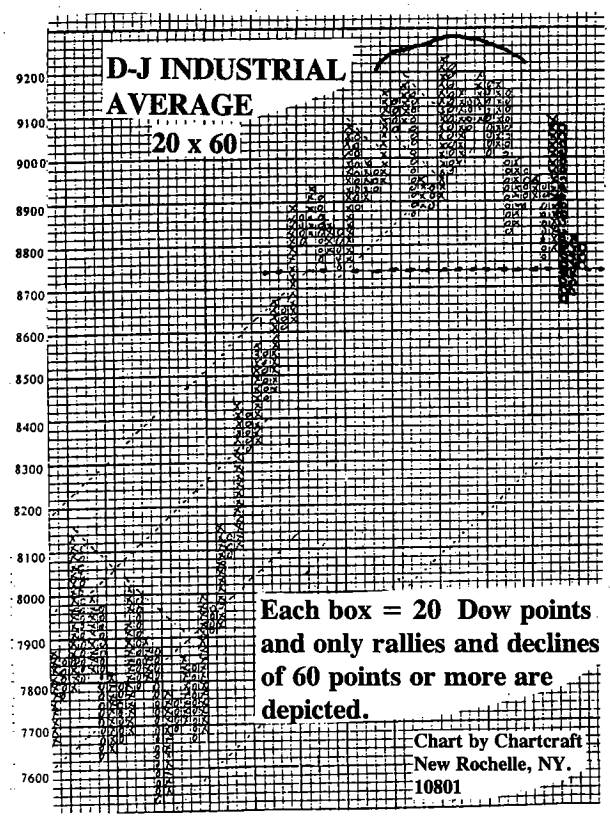
of investors are just opting for yield, I don't know. On June 10 the September bond futures rallied above their important preceding peak of April 3, thus taking the T-bond futures to their highest level since mid-January. With the yen collapsing along with Japanese and Hong Kong stocks, US bonds look to all the world like a safe harbor with attractive yields to boot. **Comment:** In case you haven't noticed, the stock market and the bonds (surprise) are de-coupling. Echoes of the '30s.

The chart on the middle of page 2 is courtesy of *United & Babson* [(781)235-0900]. It's a ratio-scaled chart of the Dow going back to the late-70s. What we see here are **three** major bull market advances. The first advance ran from 1982 to 1987 -- the 1987 crash ended that rise. The second rise began at the '87 low and continued to 1994. A one-year sideways consolidation ended that advance. The third and most explosive rise started in late-94 and has continued to the present. Note the acute, rising angle of the third advance. On the third advance the Dow advanced from 3638 (November, 1994) to 9211 (May, 1997), an amazing rise of 153% in less than three years. The

Purchasing Management Index







The next chart (*WSJ*) shows the quarterly change in pretax corporate profits. Remember, the stock market has been pricing in at least a 10% overall rise (year-over-year) in S&P earnings growth. If that perception changes, and if the new perception is that the first quarter is setting the trend for the year, then stocks could be in for trouble. The following is from the June 15 *Business Week: **"Where have all the profits gone?** What is missing from this picture? An economy that grew at 4.8% in the first quarter, unemployment down to 4.3%, and inflation that is barely visible. The answer is profits. Amid the good news, one grim detail is that, for the economy as a whole, profit growth has all but disappeared."* **Russell Comment:** And this from a magazine that is almost chronically bullish.

The chart on page 3 is a simplified picture of the Dow. It's a 20 x 60 point and figure chart. Each box on the chart equals 20 Dow points, and only rallies and declines of 60 points or more are depicted. A point and figure chart omits time and **shows only movement.** During an extended period of trading, **time elapse can obscure what is happening**. By eliminating time and showing only price action, the picture is often clarified.

My analysis of this chart is that we have a dramatic spike-rise, then a broad trading range which has assumed the form of a **huge potential top.** The limits of the trading range/top are 9260 on the upside and 8680 on the downside.On Friday (June 12) the Dow plunged to an intra-day low of 8684, then rallied back to close at 8834.94. Actually, it appears that the top broke down on June 12, but I would now want the Dow to close below 8680 before saying "look out below." Nevertheless, the chart shows a huge amount of "overhead supply." Let the traders and "bottom fishers" have their fun, but this market has been badly wounded.

This chart at the top-left of page 2 is one that I draw daily by hand (when I actually draw a chart, I get a lot better "feel" for the picture than I do when I simply punch out a chart on a computer). The chart shows the advance-decline ratio, having suffered a severe collapse, is still **lagging badly.** One problem with a breadth collapse is that it thrusts the A-D so out of kilter with the Dow that even when the market rallies, the breadth will usually fail to confirm the major averages on the upside. New highs in the Dow with the A-D refusing to confirm often leads to the formation of a major top.

Comments: I find it very unusual that the breadth has been so poor in the face of declining interest rates. It's been almost a religion in this market that declining interest rates are a bullish force for the market. I've been saying that it ain't necessarily so. In a real deflation rates can go down, with stocks heading down as well. Therefore, I think it's ominous that with bonds rising and rates declining, market breadth has been so poor (remember, up to 40% of the stocks on the NYSE are rate-sensitive and these stocks should be helped by declining rates). **Note**: Since May 5 the A-D Ratio has declined on seven out of every 10 trading days. **Second Note**: I've heard it said that there's "too much bearish talk" about the declining A-D ratio. **My view:** The direction of the majority of stocks on the NYSE is one of the **most fundamental phenomena of the market**. It's every bit as important as the direction of the major stock averages.

Russell Musing: It's almost as if we have two markets now. One, the big averages that everyone watches -- basically the Dow and to a lesser extent the S&P. The second market is the great mass of stocks as measured by the advance-decline ratios on the NYSE, the AMEX and the NASDAQ. But under the guise of strength in the Dow, the great mass of stocks has been sinking.

I do know this. Market breadth better turn around soon or it's going to drag everything down with it, the Dow, the S&Ps, profits and even business volume. There are few areas of the market or business that can withstand a persistent breadth collapse.

INVESTMENT POSITION: The bull stays in the box. Hey, this is a tough market. Aren't they all? Yeah, but this one is tougher. Here we see the bonds busting out to a five-month high, we see the rates on the long bonds dropping to 5.65%, and yet the majority of stocks have been declining. Now that's a tough market.

I've been saying for many months that I like the **bonds,** and I haven't changed my mind. Of course, when you buy government bonds, notes or bills you don't pay state taxes, but for more yield you might look at the Fannie Mae bonds, the debt of the Federal National Mortgage Assoc. This is an agency of the US government and it is one of the largest (in assets) corporations in the world. Its longer-term bonds yield over 6% and they're rated AAA.

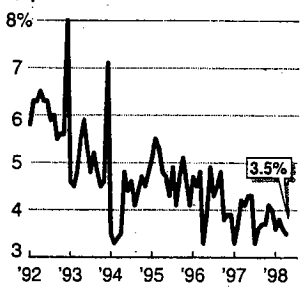
My PTI is still in the bullish mode. Although is it now definitely trending down it is still holding about 25 points above its critical 89-day moving average. If or when the primary trend of the market turns down, you will see the PTI breaking below its 89-day moving average and continuing down with a vengeance.

NOTES & QUOTES: The question I ask myself is this: "Will the collapse in Asia and Russia impact big time on the US? Or to put it another way, will the deflation which Japan and Asia are importing to the US turn into something really nasty? Ed Hyman's (*ISI*) recent charts and bulletins are eye-openers. He writes, "Judging by the decline in commodity prices, the *Journal of Commerce's* index hit a four-year low last week, the world economy is slowing down. Obviously, Asia is leading the way." He states that "over the past three weeks the odds are 50% that the US economy is slowing. Not that it is going to slow. That is already starting to slow." Hyman adds, "PAC Rim collapsing. Evidence is mounting that a number of PAC rim economies are

in depression, By that we mean real GDP declines for 1998 of roughly minus 10%, with first half declines of minus 30%. Because China's and Hong Kong's economies are deteriorating fast, we believe the odds are building that they will devalue . . . Deflation: prices of cattle in China have declined minus 65% over the past two years. Steel prices are down minus 20% year-to-year. Industrial production is declining at a minus 25% rate. Office vacancy rates are up to 70%."

Savings Rate

Savings as a percentage of disposable income



Sources: Datastream, Commerce Dept.

Russell comment: I've been warning that with one-third of the world's GDP in recession or depression, some of that is bound to rub off on the US. I'm not saying that a bear market is just around the corner, but I do know that bear markets have a nasty habit of materializing when a nation is least prepared for one. Right now, the fact is that 42% of all US families own either mutual funds or common stocks. This constitutes their savings. Aside from that, the average family has very little cash. In other words, they're loaned up -- mortgages on their homes, huge borrowings on their credit cards, loans to the banks. As far as actual savings, this chart tells the story.

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By their **currencies,** ye shall know them. This chart from the June 8 *WSJ* (it's worse now) shows the collapses in various currencies. All of which makes me think that the dollar is now too high, maybe as much as 30% too high. A lot of the dollar's strength is not because US goods are competitive, no, a lot of the strength comes from the perception that the US is safe. But if the US trade balance continues to surge negatively, I have to wonder how long the dollar can maintain its lofty perch. Remember, the more other currencies sink, the more expensive the dollar appears, at least from a trade standpoint.

The Costly Currency Impact

Many of the worst performing emerging markets since mid-1997 have had currency declines that reduced returns to U.S. investors even further in dollar terms. Percentage changes in the MSCI stock index for various markets from July 1, 1997 to June 4, 1998

MARKET	PERCENTAGE CHANGE* Local Currency	Dollar Terms
Brazil	-25.21%	-30.06%
Chile	-28.72	-34.84
Colombia	-10.38	-29.37
Greece	+61.11	+47.34
Hong Kong	-50.57	-50.59
Hungary	+48.52	+31.32
India	-14.76	-26.98
Indonesia	-46.37	-88.81
South Korea	-47.88	-66.77
Malaysia	-53.06	-70.16
Mexico	+ 7.11	- 2.64
Peru	- 14.39%	-20.23%
Philippines	- 26.91	-50.63
Poland	+ 0.46	- 4.44
Russia	- 46.86	-46.86
Singapore	- 34.26	-44.27
South Africa	- 3.87	-14.89
Taiwan	- 24.73	-38.89
Thailand	- 43.34	-65.79
Turkey	+116.33	+24.95
U.S. (DJIA)	+ 14.87	+14.87

Source: Morgan Stanley Capital International

*Percentage changes are prices only, without reinvested dividends

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A *Fortune* article (June 22) states, "Say goodbye to the last bear." It seems that Giant Canadian bank, CIBC (they bought Oppenheimer), might have "suggested" to the bearish Michael Metz that he turn in his crystal ball, and just stop forecasting. Explained Metz, "I was tired of being wrong. I'm out of sync with the modern markets. I haven't been very good lately." **Russell Comment:** There's no question that the current reigning Wall Street guru is Abbey Cohen of Goldman Sachs. In case you haven't heard, Abbey is bullish on the US stock market and doesn't believe Asia will affect our market that much. Minor prophet Richard Russell is not convinced.

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Soccer is by any count the most popular sport in the world. The latest estimate is that 250 million people around the world play the game, and this includes 30 million women. Soccer has grown at an average of 10% a year for the last 10 years. This month 32 teams are competing at 10 sites across France in what is probably the most popular sporting event in the world. An estimated 1.7 billion people will watch the World Cup championship final scheduled for July 12. This year, by the way, marks only the sixth time that the US has qualified for the World Cup finals. The US national team on February 10 played the world champion Brazilian team, and for the first time in 68 years the US won with an amazing 1-0 victory.

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University of Colorado researchers state that 54% of ALL Americans are now overweight, an increase of about 20% over the last 20 years. With this trend in place, they claim that within a few generations virtually all Americans will be overweight. Furthermore, the researchers say that 25% of American children are now overweight. The reason: Americans now eat far more than they need and exercise far less than they should. **Russell Comment:** If you're serious about losing weight my advice (from experience) is: **(1)** cut down heavily on fats, **(2)** drink a LOT of water, **(3)** go largely vegetarian, with an accent on steamed vegetables, and **(4)** definitely cut WAY down on deserts and liquor.

* *

What's wrong with Japan? A fascinating article in the June *Atlantic Monthly* by Murray Sayle provides answers: "Every distinguishing feature of the Japanese economy comes from the national theory of unity through ties of blood, and from the desperate and often semi-secret strategies devised in postwar years to exploit the theory for bare national survival. Official manipulation of markets? Families are ruled by love, not markets. Preference for costly local products over cheaper imports? Only token strikes? Families don't strike against kin? The rejection of foreign capital? Don't sell the family business to foreigners? The exclusion of immigrants and foreign 'guest workers'? Outsiders shouldn't enjoy what the Japanese have slaved to build. The equitable distribution of income? We're all Japanese here, not bosses and workers? A family owes all its members the dignity of work? Don't let the family down? A defect harms every Japanese?" Many of the above sound "nice," but they're inefficient and simply won't work in a capitalistic, free enterprise world.

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Travelers is buying 25% of Nikko securities. If 50 years ago anyone had told me that one day I'd see US companies buying up chunks of Japanese companies I would have told them they were out of their mind. World War II saw some of the bitterest fighting in the annals of history as the US fought the Japanese, island by island, hill by hill, road after road. Iwo, Tarawa, Okinawa, Guadalcanal, tens of thousands of Americans died on those islands. I asked my kids whether they had ever heard of any of those battles. Their blank faces told me the answer. Time erases all wounds. The ghastly battles fade silently into history.

One of the ironies of post-War Japan is that the Japanese (unlike the Germans) have never expressed their shame or remorse for their conduct during the war. Self-examination has not been a Japanese characteristic. The Rape of Nanking, the Death March of Bataan, the horrors of Japanese prison camps, the Japanese army's sex slaves -- the Japanese have never faced these atrocities. In fact, a new Japanese movie entitled, "Pride, the Fateful Moment," extols the virtues of General Hideki Tojo, a man who led much of Japan's war effort (he was executed in 1948 as a war criminal). In the movie, according to a *NY Times* review, "Americans are drawn as vindictive braggarts who trample over the humble and mild-mannered Japanese. The Americans shout, sweat, rage and connive. The Japanese speak politely, love deeply, and suffer their boorish conquerors with dignity." **Russell Comment**: The film is very significant. If you won't deal with your own reality, you're not going to do well in a global free-enterprise world. Of course, now we see Japan failing to deal with the reality of its sinking economy.

* *

FREE! A lot of people talk about the Federal Reserve but not many understand how it works. OK, let's make it easy. The NY Fed publishes **eight color comic books** dealing with money and the Fed. The booklets are very basic and aimed towards kids, but I think they're actually quite good (they're obviously slanted towards the kindly ol' Fed). Typical titles are "The Story of Monetary Policy," "The Story of Foreign Trade," and "The Story of Money." I liked the booklets and picked up some facts that I didn't know. Contact the Federal Reserve of NY, Public Information Dept. [(212)720-6134, (www.ny.frb.org)].

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Legal Lesson: If you need a lawyer, don't hire a family friend. Monica learned that the hard way. She must have learned, because she finally fired her nutty family lawyer, William Ginsburg. This guy was beyond incompetent. Can you believe it, Ginsburg wrote a letter to independent council Starr saying, "Congratulations, Mr. Starr! As a result of your callous disregard for cherished constitutional rights, you *may* have succeeded in unmasking a sexual relationship between two consenting adults." Unbelievable, and this after his client in an affidavit stated that she did not have a sexual relationship with "the big creep." With her new professional lawyers in charge, Monica may get immunity. If so, she will spill the beans and admit she had sex with the Prez, and if that happens Clinton will be branded as a bold-faced liar -- remember, Clinton faced the American people and stated in no uncertain terms that he did NOT have sex with "that woman". Of course, subornation of perjury is what Starr is really looking for. It's obvious that Monica is still enthralled with Bill, but I think she's going to be forced to tell the whole truth (or, of course, take the consequences).

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From Jim Stack's *InvesTech Research* [(406)862-7777]: "The four big techs -- Intel, Microsoft, Cisco Systems and Dell -- make up 23% of the NASDAQ and a whopping 43% of the reported $28.4 billion in NASDAQ profits over the past year. Without these four Wall Street 'darlings', the true P/E ratio of the remaining 5,210 stocks on the NASDAQ is (drum roll, please) . . . 96.4." **Russell Comment:** It's all part of the prevailing mania to own common stocks. But be careful, sooner or later sanity always overtakes the markets. And sanity can be painful.

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If you like income, this isn't the best of times. Only one Dow industrial stock has a dividend yield above 3%, and it's Philip Morris yielding 4.54%. Seven Dow industrials yield in the 2% area. And 14 Dow stocks yield in the 1-2% area. The remaining nine Dow industrials stocks yield less than 1%. At the bottom of the yielders is Disney at 0.57% and McDonald's at 0.52%.

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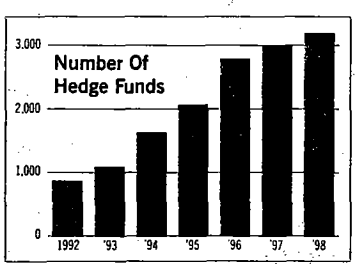
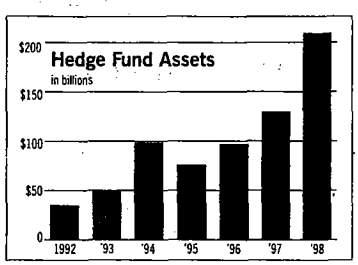
If the guys on Wall Street want to make serious money, they start a hedge fund. Hedge funds don't register with the SEC and they can do about anything they want, as long as it's legal. They can short stocks, buy coins, trade real estate, anything where they think there's a profit. There are now over 3,000 hedge funds controlling total assets of over $200 billion. This chart (courtesy of *Fortune*) tells the story.





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Last week we heard that Americans are not saving enough for their retirement. Actually, we hear a lot about retirement, and many subscribers over the years ask me when I am going to retire. I'm not going to retire. I like what I'm doing too much to retire. If I retired, I'm afraid I'd be bored to death. Even on vacations I tend to get bored after three or four days. I like my work. So when people ask, "Russell, you've been writing your Letter for forty years, give yourself a break, when are you going to retire?" I answer, "Retire to what? To doing nothing? I can't see that. Listen, if I retired I'd probably continue to read the same stuff, think the same thoughts, and lead the same life. So why retire. I don't think I could take it."

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Irony? With the **Dow** in the 8000-9000 range, Dow Jones finally gave permission to trade Diamonds -- options based on the price of the Dow. Now Waterhouse Securities has come out with a no-load mutual fund, the Dow Jones Industrial Average Index Fund, which mirrors the Dow. Ah, why weren't the Diamonds and the Dow Index Fund available years ago when the Dow was thousands of points lower? Better late than never, you say. Well, that may well be true, but one wonders, "Why now?"

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About six months ago at a big museum party here in La Jolla I won the grand prize -- two round-trip tickets via Air France to Monte Carlo, five days in the best hotel in Monte Carlo, five days in a fancy spa and a round-trip by helicopter from Monte Carlo to Nice and back. I don't like to travel. (I like getting there, but I hate the actual traveling, because it seems the planes are always late, in need of repairs, or if everything else goes right -- the flights are canceled.) At any rate, I told wife Faye, "I can't take the traveling, you go and take your sister. With four young kids, all boys, she probably needs a vacation." So sure enough, with the ladies scheduled to leave on June 8, Air France went on strike, this with the World Cup ready to go.

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Remember back a few years when the mini-Berkshires came out, at which time Warren Buffett said at that price he wouldn't buy his own stock. Wonder what he thinks now? Berkshire holdings are now worth $43 billion. But the market values them at $76 billion. That's one whopping huge premium to pay for Buffett's undoubted wisdom and leadership.

* *

I'm getting an increasing number of calls about **chelation.** Slowly, slowly, despite the opposition of the medical profession, the news is getting out. So if you have heart problems, there's something you should investigate before you submit to an operation. It's called chelation. Thanks to the Internet, there's now a lot of information you can gather about chelation. It's available on www.chelation.com. By the way, I'm still a rabid newspaper reader, but the Internet -- I'm learning to love it.

* *

Gee, I remember when **coffee** was a nickel a cup. Then coffee prices zoomed and the dirty devils raised the price to a dime a cup. And funny thing, the price of a cup of coffee never came down again. Last week coffee futures dropped to $1.20 a pound, an 18-month low. Did your neighborhood Starbucks drop the price of a decaf latte or whatever they call it? I don't think so. By the way, even the sugar you put in your coffee is cheaper now -- last week sugar futures fell to a seven-month low.

* *

The yen has now sunk to 141 to the dollar. How about this -- deposits on US dollars (90-day maturities) yield 5.875%, while at the same time 90-day paper in Japan yields 0.375%, that's around one-third of one percent in case you didn't see that decimal point. With government paper yielding almost nothing in Japan and the yen are heading south, is it any wonder that money is pouring into the US, the home of juicy-yields?

By the way, with the yen this "cheap," you have to wonder how long it will be before competitive devaluations sweep Asia again. And if they do, we'll be seeing a new flood of cheap merchandise coming to US stores (and, oh yes, also available via the Internet). And speaking of the Net, I just bought four books via the net at roughly 30% off the retail price. Add the four bucks for packing and UPS costs and it's still the way to buy books (although if you buy only one book the cost of shipping eats sharply into the discount).

* *

The *Bank Credit Analyst* and Richard Russell **agree** on the incredible importance of the Internet. In its latest issue, the *BCA*

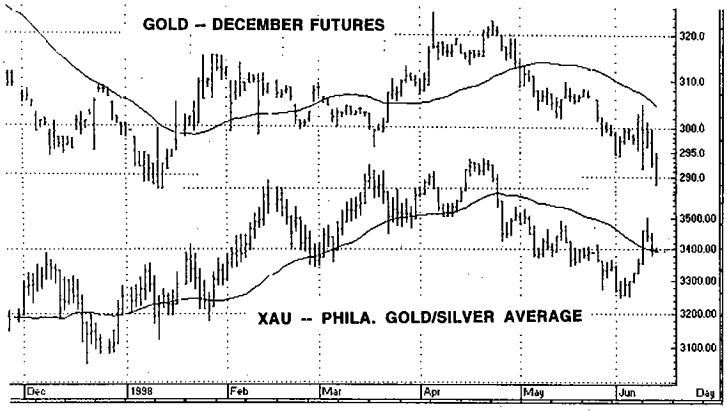
concludes, "I hope that you sense my excitement. Unfolding in front of our eyes are the early stages of the biggest fundamental change we will witness in our lives. The Internet will change almost everything from the way businesses operate to the way people interact . . . I believe the Internet will be both the central nervous system of the world economy and the epicenter of the world community."

* *

PRECIOUS METALS: Writing about the precious metals isn't much fund these days. But I've bee writing about the metals ever since 1960, through thick and thin, and this is just one of those thin times.

The top of the chart shows the December gold futures, and the best you can say here is that the futures have not yet broken below their January 13 low of 287. That's small consolation, but that's the only consolation I have here. Gold seems to be part of the global deflation trend. Let me put it this way -- if you can trade it, the odds are that it's heading down.

Everything said above applies to XAU, the Gold/Silver Average. Both gold and XAU are now well below their 34-day moving averages, which are shown on the chart.



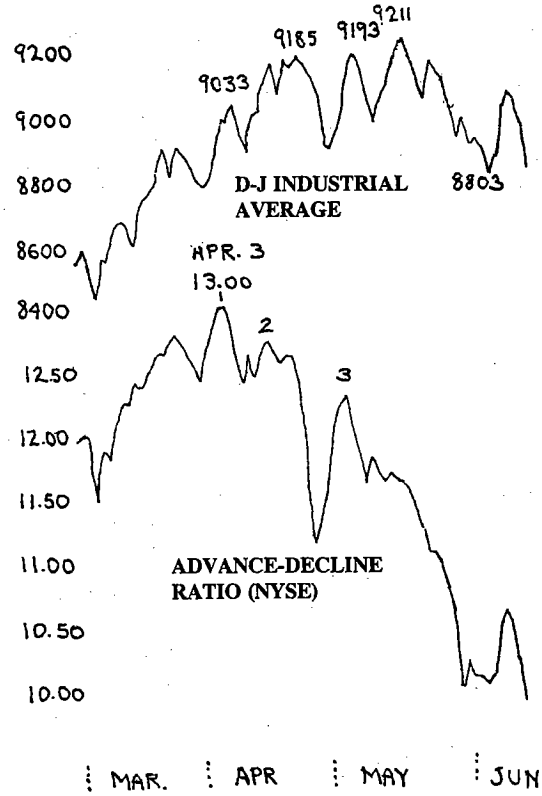
LATE NOTES: The real question we're dealing with now is whether the primary bull market is still in force, or whether the bull is slowly dying. That's the multi-trillion dollar question, and it's the question that over-rules all other questions.

Let's say that the bull still lives. If that's true, then what we've got here is a correction, a correction based pretty much on fear of the fallout from Asia -- or maybe it's a correction based on the simple thesis that the market boiler got overheated and that it just had to let off some steam. If that turns out to be the case, then the market will become oversold, it will consolidate, and in due time it will head up again to test the highs. All that is true, if we're still in a bull market. And remember, we take it to be a bull market until proved otherwise.

Now let's look at the other side of the coin. Let's say that the bull has been in the process of dying ever since April 12 (that was the day that the A-D ratio topped out). And just for argument's sake, let's say that the bear is finally waking from his long hibernation and ready to climb out of his lair. If all that is true, what can we expect?

I think what we could expect would be a stubborn, persistent collapse in breadth (of course, this is what we've seen ever since April 12). Next, I think we could see the market go over-sold (which it is now) and stay over-sold for weeks on end. Overall, I think if, and I say IF, a bear market has started we're going to see very persistent declines, declines more or less a mirror of the incredibly persistent advances that have characterized the bull market ever since the early '90s. And oh yes, if it's a bear market we can expect to see denials, nonsense, dumb statements from all quarters from Washington to CNBC, from *Business Week* to Wall Street Week.

NEXT MAILING: July 1, 1998



I'm including this up-dated chart of the Dow and the A-D ratio, a chart that appeared in the May 20 Letter. Here we see the April 3 peak in the A-D ratio, the three declining peaks against the rising peaks in the Dow. Of course this "triple divergence" tends to be a strong bearish signal, and that's been the case so far in this market. As this is written, the Dow has fallen below the June 3 low of 8803.30. I'd want the Dow to close below 8684 before I was convinced that the Dow was confirming the swooning A-D ratio on the downside.

The chart below is *Investor's Business Daily's* **Mutual Fund Index,** an index of 23 leading growth equity mutual funds. These funds, on average, are now up less than 6% in 1998, showing a return (so far) about comparable to long-term T-bonds. If the recent trend continues, and this Index drops below a zero return, I would expect fund purchases to drop drastically. Furthermore, if this is a bear market I would expect fund transactions to move to net selling. Note that the relative strength line for the Fund Index has been declining, indicating that the Funds are not keeping up with the S&Ps. I take the action of this Mutual Fund Index seriously, and it is well to remember that the great majority of these funds managers have known only bull markets (of course, that also applies to those who own the funds).